

Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-07 FRB-01
INR-07 NSAE-00 USIA-15 TRSE-00 XMB-04 OPIC-06
SP-02 LAB-04 EPG-02 SIL-01 OMB-01 AGRE-00 PA-02
PRS-01 ABF-01 ITC-01 /071 W
-----100151Z 097605 /73

R 062119Z MAY 77
FM AMEMBASSY BOGOTA
TO SECSTATE WASHDC 1392

UNCLAS BOGOTA 4196

E.O. 11652: N/A
TAGS: ECON, EFIN, CO
SUBJ: INFLATION RATE HITS RECORD HIGH

1. THE CONSUMER PRICE INDEX IN APRIL INCREASED BY A RECORD HIGH OF 7.6 PER CENT FOR WORKERS AND 6 PER CENT FOR EMPLOYEES. THE WORKER FIGURE SEASONALLY ADJUSTS TO AN ANNUAL RATE OF 50 PER CENT, AND THE FIRST FOUR MONTHS OF 1977 ADJUSTS TO A 34 PER CENT ANNUAL RATE. THE BEST MONETARY MODEL ON THE ECONOMY, BASED ON MONEY SUPPLY, INTEREST RATES AND OUTPUT, PROJECTS AN ANNUAL INFLATION RATE FOR 1977 OF 35 TO 40 PER CENT. HOWEVER, THIS MODEL DOES NOT DISTINGUISH BETWEEN AGRICULTURAL OUTPUT AND INDUSTRIAL OUTPUT, SO THAT, GIVEN THE DROUGHT, THE RATE COULD EVEN GO HIGHER.

2. THE PRICE INCREASES ARE MORE SIGNIFICANT THAN EVEN THE HISTORICAL HIGH INDICATES, BECAUSE THE PRICE CHANGES HAVE BEEN PARTICULARLY SEVERE IN BASIC STAPLES. IT IS FOR THIS REASON THAT THERE IS A LARGE DIFFERENCE BETWEEN THE WORKERS' INDEX AND THE EMPLOYEES' INDEX. THE WORKERS' INDEX IS MORE HEAVILY WEIGHTED TOWARD THE DIET AND CONSUMPTION HABITS OF THE POOR. THE FOOD COMPONENTS OF THE WORKERS' BASKET HAVE INCREASED SO FAR THIS YEAR BY 26.3 PER CENT, FOR BOGOTA DURING APRIL, BASIC ITEMS SUCH AS RICE,
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INCREASED BY 24 PER CENT, CORN BY 7.3 PER CENT, BROWN SUGAR 18.5 PER CENT, CHOCOLATE BY 75 PER CENT, YUCCA 12.4 PER CENT, POTATO BY 12.4 PER CENT AND PLATANO BY 10.3 PER CENT. THESE BASIC ITEMS CONSTITUTE PROBABLY 80 PER CENT OF THE DIET OF THE POOR. IN OTHER CITIES THE PRICE INCREASES WERE EVEN WORSE. FOR INSTANCE, THE PRICE OF PLATANO INCREASED BY 58 PER CENT IN CALI LAST MONTH AND THE PRICE OF CORN BY 28 PER CENT IN MEDELLIN.

3. AS HAS BECOME CUSTOMARY WHEN EACH MONTH'S EVEN HIGHER INFLATION RATE BECOME KNOWN, THE GOVERNMENT ANNOUNCED ANOTHER SERIES OF ANTI-INFLATIONARY MEASURES. EXPORTS OF BASIC HOUSEHOLD CONSUMPTION ITEMS SUCH AS RICE, SUGAR, CORN, MATCHES, ETC., WERE PROHIBITED, CREDIT FOR STORAGE RECEIPTS WAS ELIMINATED AND THE GOVERNMENT HAS SAID THAT IT WILL ATTEMPT TO ELIMINATE MIDDLE MEN AND SPECULATORS BY INTERVENING IN THE MARKET ON A LARGE SCALE WITH THE GOVERNMENT COMMODITIES STABILIZATION AGENCY, IDEMA.

4. COMMENT: THE RECENT EXPORT CONTROLS ARE NOT LIKELY TO HAVE A SIGNIFICANT IMPACT ON PRICES SINCE THE BORDER WITH VENEZUELA IS LONG AND CONTRABAND VOLUMINOUS. THE MEASURES TO CONTROL CREDIT FOR SPECULATION WILL HAVE LITTLE OR NO EFFECT BECAUSE, WITH A PRICE INCREASE OF OVER 10 PER CENT A MONTH FOR THESE COMMODITIES, THERE IS AMPLE CREDIT AVAILABLE. MOREOVER, IDEMA HAS BEEN NOTORIOUSLY UNSUCCESSFUL IN MOST OF ITS VENTURES, AND FEW COLOMBIANS BELIEVE THAT IDEMA CAN PLAY A CONSTRUCTIVE PRICE STABILIZING ROLE. THE GENERAL FOCUS ON SPECULATION IS MISPLACED, SINCE THE PRESENT INFLATION RATE IS A RESULT OF MONETARY EXPANSION IN LATE 1976, STRONG INTERNAL DEMAND, AND THE DROUGHT.

5. THE INFLATION THE BASIC CROPS WILL BE HARVESTED AND THE EFFECTS FROM THE NOVEMBER-DECEMBER MONETARY EXPANSION BEGIN TO DISSIPATE IN THE FIFTH AND SIXTH MONTHS. SINCE JANUARY, THE MONEY SUPPLY HAS BEEN HELD TO A 3 PER CENT GROWTH. COUNTERACTING THESE DEFLATIONARY FACTORS WILL BE THE ADJUSTMENT
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THAT THE FINANCIAL MARKETS HAVE MADE TO THE 100 PER CENT MARGINAL RESERVE REQUIREMENT, THE ARTIFICIALLY LOW INTEREST RATES, AND THE QUASI MONEY EXPANSION IN THE EXTRA BANK MARKET. SINCE BANKS CANNOT RE-LEND DEMAND DEPOSITS, THEY ARE CHANNELING MONEY INTO QUASI MONEY AND MAKING ARRANGEMENTS FOR GREATER LIQUIDITY. THUS THE ECONOMY REMAINS HIGHLY LIQUID.

6. THE RECENT MEASURES ESTABLISHING A MULTIPLE EXCHANGE RATE ARE NOW EVEN MORE LIKELY TO BE EXTENDED. THE THIRTY DAY PERIOD DURING WHICH COFFEE, SERVICE AND DEBT DOLLARS CANNOT BE TURNED INTO PESOS WILL PROBABLY BE EXTENDED TO 60 DAYS THEN 90 AND EVENTUALLY TO 120 DAYS. THIS WOULD CAUSE A 10 PER CENT REVALUATION OF THE COFFEE PESO. SINCE COFFEE PRICES ARE DECLINING, COFFEE EXPORTERS AND GROWERS WOULD REACT STRONGLY AGAINST A 10 PER CENT REVALUATION. MOREOVER, MINOR EXPORTS WOULD SUFFER. THE EXTENSION OF THE PERIOD IN WHICH DOLLARS CAN BE CHANGED INTO PESOS WITHOUT PAYING A DISCOUNT, THEREFORE, WILL PROBABLY BE ACCOMPANIED BY A GRADUAL DEVALUATION OF ABOUT 10 PER CENT FOR BOTH RATES. THE NET

EFFECT WILL BE 10 PER CENT DEVALUATION FOR THE MINOR EXPORT PESO AND LITTLE OR NO CHANGE FOR THE COFFEE PESO. THE MONE-TARY EFFECT WILL BE TO DELAY FOUR MONTHS' WORTH OF COFFEE AND SERVICE EARNINGS FROM ENTERING THE ECONOMY. THIS MEASURE, IF CARRIED OUT, WILL BE STRONGLY CONTRADICTIONARY AND WILL PUT DOWNWARD PRESSURE ON TH INFLATION RATE.

7. ON BALANCE, EVEN THOUGH THE INFLATION IS A RECORD FOR COLOMBIA, AND IS PERTICULARLY SEVERE FOR THE POOR, COLOMBIA SHOULD BE ABLE TO AVOID SLIPPING INTO A MORE DURABLE AND POLITICALLY EXPLOSIVE HYPER-INFLATION.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: INFLATION, PRICE CONTROLS
Control Number: n/a
Copy: SINGLE
Sent Date: 06-May-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment:
Disposition Date: 01-Jan-1960 12:00:00 am
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977BOGOTA04196
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D770163-0538
Format: TEL
From: BOGOTA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770587/aaaacwya.tel
Line Count: 128
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: e6c98a99-c288-dd11-92da-001cc4696bcc
Office: ACTION ARA
Original Classification: UNCLASSIFIED
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators: n/a
Previous Classification: n/a
Previous Handling Restrictions: n/a
Reference: n/a
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 28-Oct-2004 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 2621143
Secure: OPEN
Status: NATIVE
Subject: INFLATION RATE HITS RECORD HIGH
TAGS: ECON, EFIN, CO
To: STATE
Type: TE
vdkgvwkey: odb://SAS/SAS.dbo.SAS_Docs/e6c98a99-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009